

CALIFORNIA DEPARTMENT OF FOOD AND AGRICULTURE  
AUDIT OFFICE



MILK POOLING BRANCH  
MILK POOLING EQUALIZATION FUND

AUDIT REPORT  
#08-081

FISCAL YEAR ENDED JUNE 30, 2007

CALIFORNIA DEPARTMENT OF  
FOOD AND AGRICULTURE  
  
DIVISION OF MARKETING SERVICES  
MILK POOLING BRANCH  
  
MILK POOLING EQUALIZATION FUND

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REPORT NUMBER  
08-081

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## **EXECUTIVE SUMMARY**

In compliance with Section 62712(c) of the Food and Agricultural Code mandating an annual audit, we have audited the financial operation of the Milk Pooling Equalization Fund (MPEF). The audit covers the fiscal year ended June 30, 2007.

The objectives of the examination were to evaluate the internal control structure of the financial operation of the Milk Pooling Equalization Fund and to obtain reasonable assurance about whether the financial records are free of material misstatement.

## **RESULTS OF EXAMINATION**

The examination findings were discussed with Mr. Donald Shippelhoute, Senior Agricultural Economist Supervisor, and Mr. Steven Donaldson, Research Analyst II, for the Milk Pooling Branch (MPB) as items were discovered.

During our review of the internal control structure and compliance with State laws and regulations, we identified one area containing a reportable condition. The reportable condition is considered a weakness in the operation of internal controls over the Milk Pooling Equalization Fund. We have provided two recommendations to improve the operations of the fund. The MPB must respond in writing on how each recommendation will be implemented.

We also identified an additional area containing a non-reportable condition. This condition and accompanying recommendation is not considered a material weakness. We have included this item solely for the benefit of the MPB's and the CDFA Financial Services Branch's (FSB) management. We suggest the MPB and the FSB implement this recommendation as soon as practicable. The MPB and FSB, however, is not required to provide a written response to the recommendation for a non-reportable condition.

## **INTRODUCTION**

The California Department of Food and Agriculture (CDFA), Milk Pooling Branch (MPB) administers the MPEF in accordance with the Food and Agricultural Code, Division 21, Part 3, Chapter 3. The MPB is responsible for administering the Pooling Plan for fluid milk, which, together with the Dairy Marketing Branch (DMB), promotes, fosters, and encourages the intelligent production and orderly marketing of milk. Separation of duties exists in the Department for proper safeguarding of the fund. The DMB is responsible for the collection of delinquent equalization funds and assessments by handlers and the Financial Services Branch is responsible for cash receipts, deposits, cash disbursements, bank reconciliation, and maintaining the general ledger.

## **CONCLUSION**

Except for the findings described in this report, the Milk Pooling Branch and the Financial Services Branch have maintained adequate internal controls over the operation and administration of the Milk Pooling Equalization Fund. Furthermore, the financial reports reviewed were accurate in all material respects with any variances reconciled and eventually adjusted at some future date.

## **REPORTABLE CONDITIONS**

### **COLLECTION OF DELINQUENT HANDLER PAYMENTS**

A review of the MPEF's outstanding accounts receivable balances disclosed that two handlers have never remitted handler fees and have been delinquent since early 2002 and 2005, respectively. Through July 31, 2007, the total outstanding balances owed by the delinquent handlers have increased to \$461,158 and \$119,652, respectively. Collection efforts have included telephone calls, letters, administrative actions, a settlement conference, and finally, the legal actions initiated by the branch.

The MPB obtained a judgment against the first handler, after which the handler subsequently filed a notice of appeal. This handler participated in the Market Milk Pooling Plan while the delinquent balance continued to accelerate, until January 12, 2004, when the handler was declared ineligible for coverage under the Milk Producers Security Trust Fund. Currently, MPB will be working on a payment agreement with the first handler since the petition for review was denied by the Supreme Court and the court's judgment in favor of MPB still stands. This was a prior year audit finding.

In addition, CDFA served the second handler with a complaint in February 2007. Currently, the department is waiting for a court date to resolve this matter. However, it should be noted that the second handler no longer exists as a cooperative. This was a prior year audit finding.

Article 11, Section 1100 of the Market Milk Pooling Plan requires a pool manager to act for the Secretary, to the extent authorized by the Secretary, under the law in effectuating the terms and provisions of this Plan and shall perform any or all the duties authorized by the Secretary in the administration of this Plan. Such duties shall include, but are not limited to, the following:

- a. Maintain records and reports that accurately reflect the operation of the Plan, including the receipt and disbursement of all monies handled;
- b. Verify all reports and payments by each handler subject to the provisions of this Plan through audit of the books, records, and accounts of such handler, and the examination of operations or other verification deemed relevant;
- c. At the pool manager's discretion, publicly announce the name of any handler who has not made payment as required pursuant to Sections

1001, 1003, and 1005. Any handler may be excluded from the computations in determining quota and base prices if this should become necessary due to the handler's failure to comply with the payment provision specified in this paragraph.

#### *Recommendations*

- 1. The MPB should continue their collection efforts for these two delinquent handlers. Furthermore, the MPB should continue to explore and perform any other collection procedures deemed relevant as required in the administration of the Plan.*
- 2. To ensure a similar situation does not occur in the future, the MPB should review and evaluate their current policies and procedures for delinquent assessment collection. The MPB should explore requiring performance bonds, escrow deposits, or other improvements to ensure that the procedures are timely, effective, and relevant, as required by good business practices and the safeguarding of accounts receivable.*

## NON-REPORTABLE CONDITION

### BANK RECONCILIATIONS

A review of the bank account reconciliations disclosed that the Financial Services Branch did not always prepare bank reconciliations in a timely manner. Timely bank reconciliations help deter and resolve any discrepancies as they occur. In addition, bank account reconciliations were not always reviewed and approved by someone other than the preparer to indicate accuracy and timeliness of the reconciliations.

#### *Recommendation*

*The Financial Services Branch should ensure all bank reconciliations are prepared on a timely basis. The purpose of bank reconciliations is (i) to ensure that paid checks and deposits are reconciled with entries in the cash disbursements and receipts journals, (ii) to identify all current outstanding checks, (iii) to provide a comparison of bank balances to accounting records. Timely bank reconciliations can help deter and resolve any discrepancies as they occur. During the preparation and review of the reconciliations, Financial Services should ensure that all reconciling items are appropriate, and should research any item that appears irregular.*

*All bank account reconciliations should be reviewed by someone other than the preparer. The reviewer should sign and date the reconciliations to reflect that the review took place. The purpose of this review is to ensure accuracy, completeness and timeliness of the reconciliations.*



**MILK POOLING BRANCH'S RESPONSE**



CALIFORNIA DEPARTMENT OF  
FOOD & AGRICULTURE

A. G. Kawamura, Secretary

August 15, 2008

Mr. Ron Shackelford, Chief  
Audit Office  
California Department of Food & Agriculture  
1220 N Street, Rm. 344  
Sacramento, CA 95814

Dear Mr. Shackelford,

This letter is to respond to the letter from the CDFA Audit Office dated July 18, 2008. The letter was regarding the results of the audit of financial records for the Milk Pooling Branch for the fiscal period July 1, 2006 through June 30, 2007.

The two reportable conditions that were indicated in the report involved unpaid liabilities by handlers for pool obligations due the branches' equalization fund. Using the authority given to the Department by the California Food and Agricultural Code and California Milk Pooling Plan we had implemented our procedures to collect these non-payments.

Both of these incidences had been referred to the Attorney General's Office and in the instance of Organic Pastures, the Superior Court had found for the Department on the delinquency. The decision has been sustained by the Court of Appeals; and the California Supreme Court in May 2008 has chosen to not hear the case. CDFA's legal office is now in contact with Organic Pastures to enforce payment of the delinquency and for them to begin paying their current pool obligation and assessments as they occur. We recently received a full payment for the month of May 2008.

The other situation, Central Valley Dairymen (CVD), continues to be monitored by the Attorney General's Office for our interests. Mark Urban, Deputy Attorney General notified us that they have filed a claim (lien) with Stanislaus County where CVD continues to have property. Unfortunately there are other liens that are already in place, including one for \$320K. With the number of CVD legal and financial woes continuing, we do not expect an expedited conclusion to our claim. We will contact the Attorney General's office to receive an update on their attempts to obtain payment.

As mentioned in the prior audit letter we have in place, monthly procedures that address non-payment of pool obligations and assessments by handlers. When non-payments are found we have procedures in place beginning with follow-up letters leading to additional



Mr. Shackelford  
August 15, 2008  
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action including putting the offending handler on the Ineligible list for coverage of producers by the Milk Producers Security Trust Fund (MPSTF). If that is not successful we can begin the process to revoke their handler's license via an administrative hearing.

We plan to meet with our stakeholders to discuss a requirement of a performance bond or similar instrument to be drawn by handlers who have a record of being delinquent on their pool obligation and assessments.

Sincerely,



John Lee, Chief  
Milk Pooling Branch

cc: Kelly Krug, Director  
Division of Marketing Services

Don Shippelhoute, Sr. Agricultural Economist  
Milk Pooling Branch

### **CDEA EVALUATION OF RESPONSE**

A draft copy of this report was forwarded to the management of the Milk Pooling Branch, for their review and response. We have reviewed the response and it satisfactorily addresses the findings contained in this report.

## DISPOSITION OF EXAMINATION RESULTS

The findings in this management report are based on fieldwork that my staff performed from March 26, 2008 to April 11, 2008 and June 5, 2008. My staff met with management on July 2, 2008 to discuss the findings and recommendations, as well as other issues.

If you have any questions, please contact the Audit Office at (916) 651-8774.



For Ron Shackelford, CPA  
Chief, Audit Office

July 2, 2008

**REPORT DISTRIBUTION**

<u>Number</u>	<u>Recipient</u>
1	Director, CDFA Division of Marketing Services
1	Chief, Milk Pooling Branch
1	Accounting Administrator, CDFA Financial Services
1	Chief Counsel, CDFA Legal Office
1	Audit Chief, Audit Office